BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 97-239-C - ORDER NO. 2001-704

AUGUST 31, 2001

IN RE:	Proceeding to Establish Guidelines for an Intrastate Universal Service Fund.	)))	ORDER ON RECONSIDERATION

This matter comes before the Public Service Commission of South Carolina (the Commission) on various Petitions for Clarification/Rehearing/Reconsideration of Order No. 2001-419 filed on behalf of BellSouth Telecommunications, Inc. (BellSouth), the South Carolina Public Communications Association (SCPCA), the Consumer Advocate for the State of South Carolina (the Consumer Advocate), the Southeastern Competitive Carriers Association (SECCA), MCI WorldCom (WorldCom), the South Carolina Cable Television Association (SCCTA), and AT&T Communications of the Southern States, Inc. (AT&T). In addition, Returns were filed on behalf of the South Carolina Telephone Association (SCTA), and Verizon South, Inc. (Verizon). We will address each Petition individually.

BELLSOUTH PETITION

BellSouth has requested a clarification and/or reconsideration of the language contained in paragraph 11 of Order No. 2001-419. BellSouth asks that the language be revised to clarify that the Commission is adopting BellSouth's proposal, as contained in the testimony of Peter F. Martin, to make rate reductions equal to the amount of the current funding for BellSouth's Lifeline customers. Specifically, BellSouth proposes that

we delete the last two sentences of paragraph 11 of the Order and replace them with the following language:

> BellSouth is currently funding the state portion of Lifeline. In order to ensure that the implementation of the State USF does not create a windfall for the company, BellSouth has stated that it will submit to the Commission rate reductions equal to the amount of the current funding for BellSouth's Lifeline customers. See Testimony of Peter F. Martin. (Tr. Vol. III at 687). We adopt BellSouth's proposal.

SCTA supports BellSouth's requested clarification. We grant the clarification and/or reconsideration as filed. Clearly, BellSouth proposed the Lifeline equivalent rate reductions in its testimony, and we see no problem with modifying the language in paragraph 11 of Order No. 2001-419 as requested. Therefore, the last two sentences in paragraph 11 of our Order No. 2001-419 are hereby deleted, and the language as stated above shall replace those sentences.

SCPCA PETITION

SCPCA has filed two petitions in one: a Petition for Clarification and a Petition for Reconsideration. We grant clarification, but deny reconsideration.

First, in its clarification request, SCPCA requests that we further explicate our holding in Order No. 2001-419 that payphone service providers should not be required to contribute twice to the State Universal Service Fund (USF). SCPCA further notes that its proposed amendment to Section 5 of the Guidelines in this matter is clear and unopposed, in that revenues earned by local exchange carriers (LECs) and interexchange carriers (IXCs) from local and long distance charges to payphone service providers (PSPs) are not retail end user telecommunications revenues subject to USF charges. Specifically, SCPCA proposes the following amendment to Section 5 of the USF Guidelines:

> Charges by local or long distance telecommunications carriers to Payphone Service Providers (PSPs) for toll or access line charges are not retail "end user" telecommunications revenues, and do not serve as a basis for that local or long distance telecommunications carrier's contributions to the USF. As such, local and long distance telecommunications carriers are prohibited from passing any USF charges on to their PSP customers.

Although we do not necessarily agree that this language is "essential" in order to ensure that PSPs will not pay twice into the USF, we do agree that the language may be helpful in effectuating the Commission's intent to prevent such double payment from occurring, and we hereby adopt the modification to Section 5 of the Guidelines as proposed above by SCPCA.

However, we deny SCPCA's Petition for Reconsideration, which would modify the adoption of the phase one, step one plan in Order No. 2001-419. SCPCA has proposed adding to this phase a $10.88 rate reduction to BellSouth's current rate for payphone access line service (PTAS). SCPCA considers this PTAS rate an implicit subsidy that should be removed along with the reduction to switched access. SCPCA proposes that BellSouth withdraw the resulting decrease in revenues from the USF, so that the "PTAS rate reduction will be revenue-neutral for BellSouth."

As we stated in Paragraph 30 of Order No. 2001-419, it is inappropriate to reduce a PTAS rate in this Universal Service Fund proceeding. As we further noted in that Order, SCPCA's assertions would best be considered in another forum, where we are able to focus on SCPCA's specific concerns. We intend to establish that forum herein.

This Commission is very concerned over the future of the payphone industry in South Carolina, especially with the scheduled departure of BellSouth Public

Communications from the payphone business on or about December 31, 2002. Accordingly, we hereby establish a generic docket to consider the potential recovery of the Subscriber Line Charge (SLC) and the Primary Interexchange Carrier Charge (PICC) through the State Universal Service Fund. In addition, this generic docket will include the exploration of the concept of public interest payphones and the provisioning of these phones to low income areas. We believe that SCPCA's concerns and this Commission's concerns may be addressed in this generic docket.

In any event, we deny SCPCA's Petition for Reconsideration, but we establish the generic docket as outlined above.

CONSUMER ADVOCATE PETITION

The Consumer Advocate proffers a number of grounds in his Petition for Reconsideration. First, the Consumer Advocate asserts that the decision to determine the size of the USF, or to institute funding in any amount is arbitrary, capricious, contrary to the evidence of record, and in violation of other provisions of South Carolina law. This comes as somewhat of a surprise to us, considering the General Assembly's 1996 mandate to this Commission to establish a State Universal Service Fund. This is contained in S.C. Code Ann. Section 58-9-280 (E)(1)-(8)(Supp. 2000). (Subsection (E)(4) specifically states that "the size of the USF shall be determined by the Commission...") This Commission has held exhaustive proceedings over the last five years to address guidelines for administration of the State USF, cost models, and methodologies. Apparently, the Consumer Advocate would have us ignore all of our prior proceedings and the mandate of the General Assembly to implement a State Universal Service Fund.

The Consumer Advocate specifically asserts that this Commission erred in sizing the State USF because we approved a cost methodology that did not isolate the costs of providing only basic local exchange service. We would note that the determination of appropriate methodologies for calculating the cost of basic local service was made by this Commission in Order No. 98-322 in this Docket. This Order was issued on May 6, 1998, and no appeal was taken by the Consumer Advocate. Thus, the law of the case on costing has been established, and the Consumer Advocate may not now challenge our findings in that Order.

Further, even if the Consumer Advocate had properly preserved his argument, our determination regarding cost methodologies was reached after consideration of 5 days of evidence that included the testimony of 25 witnesses, including economic, financial, engineering and cost experts.

The Consumer Advocate's additional argument that access revenues should be taken into account is confusing at best. The statute requires that the State USF be calculated based on the difference between the cost of providing basic local exchange service and the "maximum amount [the carrier of last resort] may charge for the services." S.C. Code Ann. Section 58-9-280(E)(4). The statute does not say the maximum amount it may charge for the services plus the amount of any revenues received from access services. In fact, the word "revenues" does not even appear in Section 58-9-280(E)(4).

An apparently related argument made by the Consumer Advocate is that the Commission's failure to allocate the costs of the network to services other than basic

local exchange service violates Section 254(k) of the Telecommunications Act, which provides in part that services included in the definition of universal service should be bear no more than a reasonable share of the joint and common costs of facilities used to provide those services. Consumer Advocate's Petition at 4-5, paragraph 8. This matter was fully litigated and resolved in the cost proceeding in this docket. As South Carolina Telephone Coalition witness Douglas Meredith testified in March 1998, the joint and common costs were allocated to the various services using the network, in full compliance with Section 254(k) of the Act. An excerpt of Mr. Meredith's testimony regarding the South Carolina Telephone Coalition companies' embedded cost methodology illustrates the invalidity of the Consumer Advocate's allegation:

> In order to develop an embedded cost of service for residential and business one-party service, JSI used information obtained from each cost company... the financial information obtained...included booked investment amounts, including depreciation reserves, for investments under Part 32 Accounting Rules. This financial information also included allowable expense amounts for the telecommunications activity of the company. *Finally, information relating to the operation of the company that relate to how shared and common investments and expenses are allocated, and the usage of the network for various types of calling activity, was obtained.* The actual cost information is allocated to department and then to functional components within department based upon the information provided by the company. These functional components are then combined to form a basic residential or business service cost. *This procedure uses cost allocation principles that are used in embedded cost methodologies. For instance, the switching function is allocated between local and toll calls.* The only notable exception to an embedded allocation procedure that was used under our analysis is in the treatment of the loop. In the current analysis, the loop is fully allocated to the basic service. This exception is consistent with the treatment of non-traffic sensitive (NTS) loop cost by the FCC, and is consistent with the treatment used by other companies involved in this proceeding.

See Prefiled testimony of Douglas Meredith in 1998 cost proceeding at 4-5 (emphasis added). Non-rural companies and Sprint/United also allocated the costs of the network,

albeit in a different manner, by subtracting the federal support per line (calculated at 25% of the difference between the cost per line and the FCC's national revenue benchmark) from the total cost to arrive at the state support per line. See e.g., Prefiled testimony of Peter F. Martin in USF cost proceeding at 4. Based on this testimony, the Consumer Advocate's argument is without merit.

However, in support of his argument regarding an alleged violation of Section 254(k) of the Telecommunications Act of 1996, the Consumer Advocate points to the Commission's finding that it was not appropriate to allocate the costs of the telephone network to services other than basic local service. The Consumer Advocate is clearly taking the Commission's finding out of context. As indicated by the sentence following the one cited by the Consumer Advocate, this Commission was clearly discussing "loop costs." Order No. 2001-419 at 41. As stated in Meredith's testimony quoted above, fully allocating the loop (which is a direct cost, as opposed to a joint or common cost) to basic service is consistent with the treatment of non-traffic sensitive loop cost by the FCC.

The Consumer Advocate argues that the cost studies are deficient because they fail to allocate 25% of the costs to the federal jurisdiction. Again, there has been no appeal by the Consumer Advocate of Order No. 98-322, and he cannot challenge the Commission's approval of specific cost methodologies and studies now. Furthermore, it is interesting to note that, in any event, the FCC has abandoned the 25%/75% federal/state split as far as responsibility for universal service funding, and instead has left it to the states to shoulder the burden of ensuring universal service. See FCC's Ninth Report and Order and 18th Order on Reconsideration, CC Docket No. 96-45, released

November 2, 1999, at paragraph 7. In any event, as discussed in the prior paragraph, the parties did allocate a portion of the cost to the federal jurisdiction. Those companies using the BCPM model made an allocation for the portion of USF assigned to the federal jurisdiction. The methodologies put forth by the South Carolina Telephone Coalition Companies for State USF take into account and back out the actual amounts received in federal universal service funding. Thus, there can be no double recovery from the State and federal jurisdictions.

One of the more puzzling allegations of the Consumer Advocate's Petition is the assertion that there is no probative evidence in the record to support the Commission's finding that intrastate access charges are priced above cost and provide significant support for basic local exchange service. BellSouth, Verizon, Sprint, and the South Carolina Telephone Coalition all presented testimony stating that a composite access rate of 3 cents is still above cost for the companies. (Tr., Vol. II at 358; Vol. III at 669; Vol. IV at 807-08, 822-24.) Even a witness for a party opposing implementation of the State USF testified that the cost of access was $.0055. (Tr., Vol. IV at 1004, Testimony of AT&T witness Tate). The Consumer Advocate goes so far as to state that "there is no evidence in this case to support a finding that basic local exchange services are receiving any implicity subsidy at all." Consumer Advocate's Petition at 3, paragraph 7. This statement is simply not true. In the prior cost proceeding, detailed information was provided regarding the cost of providing basic local service. The cost of providing service for many companies was shown to exceed the amount the company could charge for the service by $20 to $40 or more per month. Unless these companies are losing money at

phenomenal rates, there is clearly a subsidy flowing from rates like access and other services to basic local exchange service. Furthermore, it should again be emphasized that there has been no appeal by the Consumer Advocate of Commission Order No. 98-322, approving the cost models and methodologies that provide the basis for the size of the State Universal Service Fund.

Finally, the Consumer Advocate states that this Commission cannot mandate that interexchange carriers pass through access reductions in the form of lower long distance rates. None of the interexchange carriers who are parties to this proceeding raised this issue for reconsideration. We reject the Consumer Advocate's allegation.

In sum, the Consumer Advocate's Petition is denied.

SECCA PETITION

The Southeastern Competitive Carriers Association, WorldCom, Inc., and the South Carolina Cable Television Association filed a joint Petition for Rehearing or Reconsideration. This will be referred to hereinafter as the SECCA Petition, and the parties will be referred to collectively as SECCA. We grant in part and deny in part the SECCA Petition as will be explained below.

First, SECCA asserts that Commission Order No. 2001-419 fails to establish the size of the State USF, in violation of State law. Unfortunately, SECCA fails to acknowledge that the Commission previously sized the State USF using the statutory formula in our earlier cost proceeding in this Docket. Order No. 2001-419 orders implementation of the initial step of the State USF in the amount of approximately $38.4 million, or the amount necessary to fund access reductions by all incumbent LECs of

approximately 50% or to a composite rate of approximately 3 cents for both originating and terminating access. Order No. 2001-419 further sets up a process whereby LECs can, upon a detailed cost showing that implicit support exists in particular rates, reduce those rates and receive additional universal service funding for the removal of that implicit support. We believe that our approach was cautious and well-reasoned, since it establishes the amount of the State USF for the initial phase of implementation, and sets forth a process whereby the LECs can gradually identify and reduce the implicit support in other rates. Thus, the assertion of SECCA must be rejected.

Next, SECCA argues that the State USF is a barrier to entry because it permits incumbent LECs to "protect themselves from competition." To the contrary and as contemplated by the Telecommunications Act of 1996, the removal of implicit support in rates allows incumbent LECs to compete on a level playing field with competitive carriers who are not subject to the effects of historical residual price-setting. CLECs do not have an obligation to provide basic local exchange service at rates that are below the company's cost, as ILECs do, and thus do not have implicit support built into other rates. This is exactly the situation Congress was attempting to redress in providing for federal and State Universal Service Funding and the removal of implicit support in rates for services other than basic local exchange service. Therefore, there is no validity to the statement that the State USF is a barrier to entry because it affords "protection from competition" for the ILECs.

Further, SECCA alleges that the State USF is oversized because the Commission's approach in calculating the State USF mismatches costs and revenues by

using all of the costs associated with the facilities and only the revenues received from the basic local service. Again, there was no appeal by SECCA of Order No. 98-322, which approved cost models and methodologies to be used in sizing the State USF. SECCA may not therefore raise issues addressed by that Order in this portion of the case. In addition, even if it could, State law requires that the Commission size the State USF based on the difference between the cost of providing basic local exchange service and the maximum amount the carrier of last resort may charge for such service. The statute makes no provision for a consideration of "revenues," especially from services other than basic local service. This SECCA allegation is therefore without merit.

An additional assertion of SECCA is that the State USF is discriminatory because it permits withdrawal of funds only upon a showing that a local exchange company has reduced rates to remove implicit subsidies and, therefore, only incumbent LECs can withdraw from the State USF. This argument ignores the fact that State USF funding is portable, and that CLECs can withdraw from the State USF upon an appropriate showing. Initially, ILECs are the carriers of last resort in their respective service areas because they are the carriers that have undertaken the obligation to provide basic local exchange service to all requesting customers in those areas. However, CLECs may qualify as carriers of last resort upon an appropriate showing, according to the State USF Guidelines adopted by the Commission. Once a CLEC qualifies as a carrier of last resort, State USF funds are portable to that CLEC as provided for in the Guidelines. This is consistent with the purpose behind the State USF to ensure the continued provision of basic local exchange telephone service at affordable rates. If a particular CLEC is not eligible to

draw from the fund, it is only because that CLEC has not undertaken an obligation to provide universal service. Accordingly, the State USF is not discriminatory.

Further, SECCA alleges that Order No. 2001-419 conflicts with Federal law in contravention of the Federal Telecommunications Act of 1996 in its attempt to assess contributions to the State USF on interstate revenues. According to SECCA, interstate revenues are subject to a federal surcharge to support the federal USF, and the USF of Order No. 2001-419 impermissibly burdens federal universal service support mechanisms in violation of 47 USC Section 254(e) by imposing an additional state surcharge on those same interstate revenues. This allegation is without merit. We based our determination of this issue on a reasoned analysis of applicable law, and found that it was reasonable to include interstate revenues in the base of revenues on which State USF contributions are calculated. See Order No. 2001-419 at 37, paragraph 16. We noted that the revenues to be included are billed to end users *in the State of South Carolina*, and that both intrastate and interstate telecommunications services sold in South Carolina will benefit from Universal Service and should share in contributing to the State USF.

Finally, as SECCA notes in Paragraph 19 of Order No. 2001-419, this Commission adopted the recommendations of several parties that companies should be authorized to recover contributions to the USF through the use of a uniform percentage surcharge on end-user retail revenues. SECCA states that while a Company may have the option of whether or not to attempt to recover such contributions, if it decided to do so, SECCA believes that we intended to mandate the utilization of a surcharge. For clarification, SECCA requests that a sentence be added at the end of paragraph 19

providing as follows: "Therefore, any company attempting to recover contributions to the State Universal Service Fund shall do so through the use of a uniform percentage surcharge on end-user retained revenues." We grant clarification, and grant SECCA's request. We agree that our intent was to have anyone who exercises its option to recover contributions to the State USF to utilize the surcharge set out in our original Commission Order No. 2001-419. Accordingly, the sentence requested by SECCA as stated above is hereby added to the end of paragraph 19 of Order No. 2001-419.

Accordingly, SECCA's Petition is granted in part and denied in part.

AT&T PETITION

First, AT&T raises a ground similar to SECCA, i.e., that the Commission's decision to include revenues from interstate revenues for interstate telecommunications services in the base of contributions for the State USF exceeds the Commission's jurisdiction and improperly impairs interstate commerce. We disagree with and reject this assertion, based on the reasoning stated above in response to the SECCA Petition, and the language quoted from Order No. 2001-419.

Next, AT&T asserts that this Commission erred in failing to immediately transition the Interim LEC Fund into the State USF. This ground is without merit. As we properly found, the State USF is neither finalized nor adequate to support the obligations of the Interim LEC Fund, as required by S.C. Code Ann. Section 58-9-280(M). Thus, a transition of the Interim LEC Fund into the State USF is neither practical nor reasonable at this time.

AT&T also argues, apparently for the first time, that the Interim LEC Fund constitutes a "barrier to entry" because it is available only to incumbent LECs and not to competitive LECs. AT&T did not make this argument during the hearing on this matter. A Petition for Rehearing or Reconsideration "shall set forth...[t]he alleged error or errors in the Commission Order." S.C. Code Ann. Regs. 103-836(4)(b). The Commission cannot err with respect to an argument that was not presented during the hearing or in a post-hearing legal brief. However, even if the argument had been properly raised, it has no merit. The Interim LEC Fund was established by the Commission pursuant to a directive of the South Carolina General Assembly in order to bring about comparability of access rates among incumbent LECs in South Carolina. The Interim LEC Fund is a State fund created by State law for a specific purpose. It does not serve the same purpose as a Universal Service Fund.

Finally, AT&T requests that this Commission clarify that companies attempting to recover contributions to the State USF shall do so through the use of a uniform percentage surcharge on end-user retail revenues. As noted above, in our discussion of a similar point in the SECCA Petition, we agree with this assertion, and have ordered a modification to Paragraph 19 of Order No. 2001-419 to reflect our agreement with this proposition. This modification is consistent with that requested by AT&T. Accordingly, we grant AT&T's request for clarification on this point.

CONCLUSION

We trust that we have addressed all of the concerns of the parties in this matter. Our goal in this Order was to clarify, when necessary, our directives in Order No. 2001-419, and to complete the establishment of the State Universal Service Fund in concert with our mandate from the South Carolina General Assembly. We believe that we have met that goal. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Chairman

ATTEST:

Executive Director

(SEAL)